

Auditing Procedures Report

Issued under P.A. 2 of 1968, as amended and P.A. 71 of 1919, as amended.

Local Unit of Government Type <input type="checkbox"/> County <input type="checkbox"/> City <input type="checkbox"/> Twp <input type="checkbox"/> Village <input checked="" type="checkbox"/> Other		Local Unit Name Battle Creek Unlimited - Loan Funds	County Calhoun
Fiscal Year End June 30, 2006	Opinion Date September 28, 2006	Date Audit Report Submitted to State December 6, 2006	

We affirm that:

We are certified public accountants licensed to practice in Michigan.

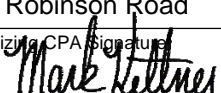
We further affirm the following material, "no" responses have been disclosed in the financial statements, including the notes, or in the Management Letter (report of comments and recommendations).

YES ☒ NO ☐ Check each applicable box below. (See instructions for further detail.)

1. ☒ ☐ All required component units/funds/agencies of the local unit are included in the financial statements and/or disclosed in the reporting entity notes to the financial statements as necessary.
2. ☒ ☐ There are no accumulated deficits in one or more of this unit's unreserved fund balances/unrestricted net assets (P.A. 275 of 1980) or the local unit has not exceeded its budget for expenditures.
3. ☒ ☐ The local unit is in compliance with the Uniform Chart of Accounts issued by the Department of Treasury.
4. ☒ ☐ The local unit has adopted a budget for all required funds.
5. ☒ ☐ A public hearing on the budget was held in accordance with State statute.
6. ☒ ☐ The local unit has not violated the Municipal Finance Act, an order issued under the Emergency Municipal Loan Act, or other guidance as issued by the Local Audit and Finance Division.
7. ☒ ☐ The local unit has not been delinquent in distributing tax revenues that were collected for another taxing unit.
8. ☒ ☐ The local unit only holds deposits/investments that comply with statutory requirements.
9. ☒ ☐ The local unit has no illegal or unauthorized expenditures that came to our attention as defined in the *Bulletin for Audits of Local Units of Government in Michigan*, as revised (see Appendix H of Bulletin).
10. ☒ ☐ There are no indications of defalcation, fraud or embezzlement, which came to our attention during the course of our audit that have not been previously communicated to the Local Audit and Finance Division (LAFD). If there is such activity that has not been communicated, please submit a separate report under separate cover.
11. ☒ ☐ The local unit is free of repeated comments from previous years.
12. ☒ ☐ The audit opinion is UNQUALIFIED.
13. ☒ ☐ The local unit has complied with GASB 34 or GASB 34 as modified by MCGAA Statement #7 and other generally accepted accounting principles (GAAP).
14. ☒ ☐ The board or council approves all invoices prior to payment as required by charter or statute.
15. ☒ ☐ To our knowledge, bank reconciliations that were reviewed were performed timely.

If a local unit of government (authorities and commissions included) is operating within the boundaries of the audited entity and is not included in this or any other audit report, nor do they obtain a stand-alone audit, please enclose the name(s), address(es), and a description(s) of the authority and/or commission.

I, the undersigned, certify that this statement is complete and accurate in all respects.

We have enclosed the following:	Enclosed	Not Required (enter a brief justification)		
Financial Statements	<input checked="" type="checkbox"/>			
The letter of Comments and Recommendations	<input checked="" type="checkbox"/>			
Other (Describe)	<input type="checkbox"/>			
Certified Public Accountant (Firm Name) Rehmann Robson		Telephone Number 517-787-6503		
Street Address 675 Robinson Road		City Jackson	State MI	Zip 49203
Authorizing CPA Signature 		Printed Name Mark T. Kettner, CPA, CGFM		License Number 11673

**CITY OF BATTLE CREEK
LOAN FUNDS ADMINISTERED BY
BATTLE CREEK UNLIMITED, INC.**

Battle Creek, Michigan

Financial Statements

**For the Year Ended
June 30, 2006**



REHMANN ROBSON

Certified Public Accountants

**CITY OF BATTLE CREEK LOAN FUNDS
ADMINISTERED BY BATTLE CREEK UNLIMITED, INC.**

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REHMANN ROBSON

Certified Public Accountants

A member of THE REHMANN GROUP



Independent Auditors' Report

September 28, 2006

Honorable Mayor and Members of
the City Commission
City of Battle Creek, Michigan

We have audited the accompanying financial statements of the ***City of Battle Creek Loan Funds Administered by Battle Creek Unlimited, Inc.*** (which consists of an enterprise fund of the City of Battle Creek, Michigan and an enterprise fund of the Battle Creek Downtown Development Authority, a component unit of the City of Battle Creek, Michigan) as of and for the year ended June 30, 2006, as listed in the table of contents. These financial statements are the responsibility of Battle Creek Unlimited, Inc.'s management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the City of Battle Creek Loan Funds Administered by Battle Creek Unlimited, Inc. and do not purport to, and do not present fairly the financial position of either the City of Battle Creek, Michigan or the Battle Creek Downtown Development Authority, and the changes in their financial position and their cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the City of Battle Creek Loan Funds Administered by Battle Creek Unlimited, Inc. as of June 30, 2006, and the changes in financial position thereof and their cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

FINANCIAL STATEMENTS

City of Battle Creek Loan Funds
Administered by Battle Creek Unlimited, Inc.
Statement of Net Assets
June 30, 2006

	Economic Development Fund	Downtown Development Authority Revolving Loan Fund
Assets		
Cash and cash equivalents	\$ 966,313	\$ 162,456
Investments	5,954,223	263,227
Loans receivable, current portion, net	2,231,680	37,331
Accrued interest receivable	55,801	5,469
Due from Battle Creek Unlimited, Inc.	-	1,009,528
Due from DDA Revolving Loan Fund	278,544	-
	<hr/>	<hr/>
Total current assets	9,486,561	1,478,011
Loans receivable, less current portion, net	3,209,896	462,575
	<hr/>	<hr/>
Total assets	12,696,457	1,940,586
	<hr/>	<hr/>
Liabilities		
Due to Battle Creek Unlimited, Inc.	3,254,027	-
Due to City of Battle Creek	-	199,996
Due to Economic Development Fund	-	278,544
	<hr/>	<hr/>
Total liabilities	3,254,027	478,540
	<hr/>	<hr/>
Net assets		
Unrestricted	\$ 9,442,430	\$ 1,462,046
	<hr/>	<hr/>

The accompanying notes are an integral part of these financial statements.

City of Battle Creek Loan Funds
Administered by Battle Creek Unlimited, Inc.
Statement of Revenue, Expenses
and Changes in Net Assets
For the Year Ended June 30, 2006

	Economic Development Fund	Downtown Development Authority Revolving Loan Fund
Operating revenues		
Interest on loans	\$ 117,934	\$ 7,772
Loan fees	770	661
	<hr/>	<hr/>
Total operating revenues	118,704	8,433
	<hr/>	<hr/>
Operating expenses		
Administration	97,500	32,500
Other operating costs	46,852	1,921
Loan loss provision	545,760	31,600
	<hr/>	<hr/>
Total operating expenses	690,112	66,021
	<hr/>	<hr/>
Operating income (loss)	(571,408)	(57,588)
	<hr/>	<hr/>
Nonoperating revenues		
Investment earnings	212,189	13,313
	<hr/>	<hr/>
Change in net assets	(359,219)	(44,275)
	<hr/>	<hr/>
Net assets, beginning of year	9,801,649	1,506,321
	<hr/>	<hr/>
Net assets, end of year	<u><u>\$ 9,442,430</u></u>	<u><u>\$ 1,462,046</u></u>

The accompanying notes are an integral part of these financial statements.

City of Battle Creek Loan Funds
Administered by Battle Creek Unlimited, Inc.
Statement of Cash Flows
For the Year Ended June 30, 2006

	Economic Development Fund	Downtown Development Authority Revolving Loan Fund
Cash flows from operating activities		
Loans collected from borrowers	\$ 1,126,437	\$ 24,668
Interest and fees on loans	118,704	8,433
Loans made to borrowers	(659,286)	(111,317)
Administrative and other expense paid	-	(135)
	<hr/>	<hr/>
Net cash provided by (used for) operating activities	585,855	(78,351)
	<hr/>	<hr/>
Cash flows from investing activities		
Purchase of investments	(1,121,727)	(49,742)
Proceeds from sale and redemption of investments	982,182	44,853
Investment income received	193,581	11,472
	<hr/>	<hr/>
Net cash provided by (used for) investing activities	54,036	6,583
	<hr/>	<hr/>
Net (increase) decrease in cash and cash equivalents	639,891	(71,768)
	<hr/>	<hr/>
Cash and cash equivalents, beginning of year	326,422	234,224
	<hr/>	<hr/>
Cash and cash equivalents, end of year	<u><u>\$ 966,313</u></u>	<u><u>\$ 162,456</u></u>
Reconciliation of operating income (loss) to net cash provided by (used for) operating activities		
Operating income (loss)	\$ (571,408)	\$ (57,588)
Adjustments to reconcile operating income (loss) to net cash provided by (used for) operating activities:		
Change in assets and liabilities:		
Loans receivable	996,805	(287,863)
Due from Battle Creek Unlimited	-	34,286
Due from DDA Revolving Loan Fund	(32,818)	-
Due to Battle Creek Unlimited	193,276	-
Due to City of Battle Creek	-	199,996
Due to Economic Development Fund	-	32,818
	<hr/>	<hr/>
Net cash provided by (used for) operating activities	<u><u>\$ 585,855</u></u>	<u><u>\$ (78,351)</u></u>

The accompanying notes are an integral part of these financial statements.

CITY OF BATTLE CREEK LOAN FUNDS ADMINISTERED BY BATTLE CREEK UNLIMITED, INC.

Notes to Financial Statements

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The City of Battle Creek Loan Funds Administered by Battle Creek Unlimited, Inc. (the “Loan Funds”) consists of the Economic Development Fund, an enterprise fund of the City of Battle Creek, Michigan (the “City”), and the Downtown Development Authority Revolving Loan Fund, an enterprise fund of the Battle Creek Downtown Development Authority (the “DDA”), a component unit of the City of Battle Creek, Michigan. The Loan Funds provide financing to businesses to create and retain jobs in the City and DDA district, respectively.

The net assets of the Economic Development Fund are the property of the City of Battle Creek; the fund was originally created by an appropriation from the City. The net assets of the Downtown Development Authority Revolving Loan Fund are the property of the DDA; the fund was originally created by a grant received by the DDA from the Miller Foundation. Both the City and DDA contract with Battle Creek Unlimited, Inc. to administer these funds.

The accounting policies of the Loan Funds conform with generally accepted accounting principles as applicable to proprietary funds. A summary of significant accounting policies follows.

Reporting Entity - These financial statements present the financial position, changes in financial position and cash flows of an enterprise fund of the City and an enterprise fund of the DDA; both funds are an integral part of the respective reporting entities. The Loan Funds are not a component unit of the City, DDA or any other reporting entity, as defined by Governmental Accounting Standards Board (GASB) Statement No. 14, *The Financial Reporting Entity*.

Basis of Accounting - The Loan Funds are separate accounting entities with self-balancing set of accounts used to report financial position, changes in financial position and cash flows. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain governmental functions and activities.

The Loan Funds are operated as enterprise funds, which are used to account for those operations that are financed and operated in a manner similar to private business or where the governing body has decided that the determination of revenues earned, costs incurred and/or net income is necessary for management accountability. Enterprise funds are accounted for on the flow of economic resources measurement focus and use the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. The Loan Funds apply all applicable FASB pronouncements issued through November 30, 1989 in accounting and reporting for their proprietary operations, but have elected not to follow subsequent private-sector guidance.

**CITY OF BATTLE CREEK LOAN FUNDS
ADMINISTERED BY BATTLE CREEK UNLIMITED, INC.**

Notes to Financial Statements

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The operating revenues of the City of Battle Creek Loan Funds Administered by Battle Creek Unlimited, Inc. include interest on loans, loan fees and other revenue. Operating expenses of the enterprise funds include administration, a loan loss provision/recovery and other operating costs. All revenue and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Deposits and Investments – The Loan Funds' cash and cash equivalents consist of demand deposits. Investments are stated at fair value and consist of U.S. treasury notes and other U.S. government obligations.

State statutes authorize local governments to deposit in the accounts of federally insured banks, credit unions, and savings and loan associations, and to invest in obligations of the U.S. Treasury, certain commercial paper, repurchase agreements, bankers acceptances, and mutual funds composed of otherwise legal investments.

Loans Receivable – Loans receivable consist of balances outstanding from borrowers and are reported net of amounts estimated to be uncollectible.

Net Assets – Restricted net assets represent amounts that are committed for either approved loan applications or minority lending.

2. DEPOSITS AND INVESTMENTS

Deposits – At year-end, the carrying amount of the Economic Development Fund's deposits were \$966,313 and the bank balance was \$964,956. Of the bank balance, \$864,956 was uninsured and uncollateralized. Also at year-end, the carrying amount of the DDA Revolving Loan Fund's deposits were \$162,456 and the bank balance was \$162,456. Of the bank balance, \$62,456 was uninsured and uncollateralized.

The government believes that due to the dollar amounts of cash deposits and the limits of FDIC insurance, it is impractical to insure all bank deposits. As a result, the government evaluates each financial institution with which it deposits government funds and assesses the level of risk of each institution; only those institutions with an acceptable estimated risk level are used as depositories.

CITY OF BATTLE CREEK LOAN FUNDS
ADMINISTERED BY BATTLE CREEK UNLIMITED, INC.

Notes to Financial Statements

At year end, the Loan Funds' investment balances were as follows:

<u>Category</u>	<u>Fair Value</u>
U.S. treasuries	\$ 1,720,631
U.S. agencies	3,346,156
Money market funds	<u>1,150,663</u>
Total investments	<u>\$ 6,217,450</u>

Credit Risk. All of the Loan Funds' investments in debt securities of U.S. agencies are rated AAA by both Moody's Investor Service. The money market funds were rated Aaa by Moody's .

Custodial Credit Risk. For investments, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Loan Funds will not be able to recover the value of their investments or collateral securities that are in the possession of an outside party. Although uninsured and unregistered, the Loan Funds' investments are not exposed to custodial credit risk since the securities are held by the counterparty's trust department in the Loan Funds' name.

Concentration of Credit Risk. At June 30, 2006, the investment portfolio of U.S. agencies was concentrated as follows:

<u>Investment Type</u>	<u>Issuer</u>	<u>% of Portfolio</u>
U.S. agencies	Federal National Mortgage Association	4.9%
	Federal Home Loan Mortgage Association	7.9%
	Federal Home Loan Bank	23.9%
	Federal Farm Credit Bank	29.4%

**CITY OF BATTLE CREEK LOAN FUNDS
ADMINISTERED BY BATTLE CREEK UNLIMITED, INC.**

Notes to Financial Statements

Interest Rate Risk. As of June 30, 2006, maturities of the City of Battle Creek's Loan Funds investments in debt securities were as follows:

		Investment Maturities (fair value by years)	
	<u>Fair Value</u>	<u>Less Than 1</u>	<u>1-5</u>
U.S. treasuries	\$ 1,720,631	\$ 645,970	\$ 1,074,661
U.S. agencies	<u>3,346,156</u>	<u>2,434,714</u>	<u>911,442</u>
	<u>\$ 5,066,787</u>	<u>\$ 3,080,684</u>	<u>\$ 1,986,103</u>

None of the U.S. agencies securities is callable.

3. LOANS OUTSTANDING

Loans receivable outstanding as of June 30, 2006, are summarized as follows:

	<u>Economic Development Fund</u>	<u>DDA Revolving Loan Fund</u>
Total loans outstanding	\$ 5,764,993	\$ 629,506
Allowance for loan losses	<u>323,417</u>	<u>129,600</u>
Net loans outstanding	5,441,576	499,906
Less amounts expected to be collected within one year	<u>2,231,680</u>	<u>37,331</u>
Amounts expected to be collected beyond one year	<u>\$ 3,209,896</u>	<u>\$ 462,575</u>

Included in the Economic Development Fund's amounts expected to be collected beyond one year are four loans made to Battle Creek Unlimited, Inc. The total amount of these loans is \$1,965,000.

* * * * *



REHMANN ROBSON

Certified Public Accountants

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September 28, 2006

To the Honorable Mayor and City Commissioners
of the City of Battle Creek and the Loan Committee
of Battle Creek Unlimited, Inc.
Battle Creek, Michigan

We have audited the financial statements of the Loan Funds Administered by Battle Creek Unlimited, Inc. for the year ended June 30, 2006, and have issued our report thereon dated September 28, 2006. Professional standards require that we provide you with the following information related to our audit.

Our Responsibility Under Auditing Standards Generally Accepted in the United States of America

As stated in our engagement letter dated July 26, 2006, our responsibility, as described by professional standards, is to plan and perform our audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement and are fairly presented in accordance with accounting principles generally accepted in the United States of America. Because an audit is designed to provide reasonable, but not absolute assurance and because we did not perform a detailed examination of all transactions, there is a risk that material misstatements may exist and not be detected by us.

As part of our audit, we considered the internal control of the Loan Funds Administered by Battle Creek Unlimited, Inc. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

Significant Accounting Policies

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we advised management about the appropriateness of accounting policies and their application. The significant accounting policies used by the Loan Funds Administered by Battle Creek Unlimited, Inc. are described in Note 1 to the financial statements.

We noted no transactions entered into by the Loan Funds Administered by Battle Creek Unlimited, Inc. during the year that were both significant and unusual, and of which, under professional standards, we are required to inform you, or transactions for which there is a lack of authoritative guidance or consensus.

Accounting Estimates

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements were:

- Management's estimate of the collectability of loans receivable. We evaluated the key assumptions used to develop the allowance for doubtful accounts to determine that they are reasonable in relation to the financial statements taken as a whole.

Audit Adjustments

For purposes of this letter, professional standards define an audit adjustment as a proposed correction of the financial statements that, in our judgment, may not have been detected except through our auditing procedures. An audit adjustment may or may not indicate matters that could have a significant effect on the City's financial reporting process (that is, cause future financial statements to be materially misstated). In our judgment, none of the adjustments we proposed, whether recorded or unrecorded by the Loan Funds, either individually or in the aggregate, indicate matters that could have a significant effect on the Loan Funds' financial reporting process.

Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the governmental unit's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Issues Discussed Prior to Retention of Independent Auditors

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the Loan Fund's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Difficulties Encountered in Performing the Audit

We encountered no difficulties in dealing with management in performing our audit.

This report and the accompanying memorandum are intended solely for the information and use of the Loan Committee and management of the Loan Funds Administered by Battle Creek Unlimited, the State of Michigan, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

A handwritten signature in black ink that reads "Lehmann Johnson". The signature is written in a cursive, flowing style with a large initial 'L'.

Loan Funds Administered by Battle Creek Unlimited, Inc.

Comments and Recommendations

For the Year Ended June 30, 2006

During our audit we became aware of certain issues regarding internal control and financial reporting. This memorandum summarizes our comments and suggestions regarding these matters. This memorandum does not affect our report dated September 28, 2006 on the financial statements of the Loan Funds Administered by Battle Creek Unlimited, Inc.

Internal Controls – Segregation of Duties

Management is responsible for establishing and maintaining effective internal control over financial reporting and the safeguarding of the Loan Funds' assets. In establishing appropriate internal controls, careful consideration must be given to the cost of a particular control and the related benefits to be received. Accordingly, management must make the difficult decision of what degree of risk it is willing to accept, given the government's unique circumstances.

As is the case with many organizations of similar size, Battle Creek Unlimited, Inc. lacks a sufficient number of accounting personnel in order to ensure a complete segregation of duties within its accounting function. Ideally, no single individual should ever be able to authorize a transaction, record the transaction in the accounting records, and maintain custody of the assets resulting from the transaction. Effectively, proper segregation of duties is intended to prevent an individual from committing an act of fraud or abuse and being able to conceal it.

Events of recent years have given rise to a heightened awareness of the risks of fraud and abuse, especially in the governmental environment, where public accountability is at its highest. The purpose of internal controls is to provide reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are properly authorized and recorded. Any limitations on the effectiveness of a government's internal controls carries with it a greater risk of fraud and abuse.

As stated previously, the establishing and maintaining of internal controls is the responsibility of management. As the Loan Funds' independent external auditors, we are specifically banned by professional standards from performing any management functions. In other words, the annual audit is not a part of the Loan Funds' internal control structure, and cannot not be relied upon as part of *management's* systems to deter or detect fraud and abuse.

While there are, of course, no easy answers to the challenge of balancing the costs and benefits of internal controls and the segregation of duties, we would nevertheless encourage management to actively seek ways to further strengthen its internal control structure by requiring as much independent review, reconciliation, and approval of accounting functions by qualified members of management as possible.

Other Internal Control Considerations

Currently, the same individual receipts checks received via the mail and over the counter and prepares the bank deposit. In order to enhance the internal controls in this area, we recommend that another individual in the Finance Department agree the deposit slip with the cash received log. We are pleased to note that the Finance Department intends to implement this new control immediately.

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